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CLERK

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1943

No. 502

BERNARD EUGENE SMITH, ET AL., AS CO-PARTNERS, TRADING AND DOING BUSINESS UNDER THE FIRM NAME AND STYLE OF THOMSON & McKINNON,

Appellants,

vs.

J. N. LUMMUS, JR., AS TAX ASSESSOR OF DADE COUNTY, FLORIDA, ET AL.

APPEAL FROM THE SUPREME COURT OF THE STATE OF FLORIDA.

APPELLANT'S BRIEF OPPOSING MOTION TO DISMISS.

GEORGE H. SALLEY,
CHARLES A. CARROLL,
Counsel for Appellants.

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vs.

J. N. LUMMUS, JR., AS TAX ASSESSOR OF DADE COUNTY, FLORIDA, ET AL.,

Appellees.

MEMORANDUM BRIEF OPPOSING APPELLEES' MOTION TO DISMISS.

(Under Rule 7, Paragraph 3.)

I.

Federal Questions Were Raised and Decided in the State Court.

The contention of the Appellees that no federal questions were raised or decided by the Supreme Court of Florida upon the second appeal because said Court failed, in its opinion, specifically to discuss the federal questions, when deciding the case on its merits, is wholly unsound.

The federal questions were, at the outset, raised in Paragraph 8 of the bill of complaint in the following language:

> "Plaintiffs charge the contrary, and allege that such property is not within the jurisdiction of this State, and that if said statute is interpreted and applied to provide for or authorize taxation of such debit balances, it results in laying a tax on property wholly beyond the jurisdiction of the State, and consequently offends the 14th Amendment of the Federal Constitution and Section 12 of the Declaration of Rights of the Constitution of Florida by depriving the Plaintiffs of property without due process of law, and further violates such provision of the Federal Constitution by denying to Plaintiffs within the State of Florida the equal protection of the laws, and also violates the Commerce Clause of the Federal Constitution (Art. I, Sec. 8, Cl. 3) by imposing a direct burden upon interstate commerce."

These federal questions were again raised in the Supreme Court of Florida upon the first appeal of this case to said Court. The Supreme Court of Florida was fully cognizant of the fact that federal questions were involved as shown by its reference to some of them in the first opinion rendered in this case, by direct reference, as well as by the holding of the Court that to sanction the attempted taxation on the facts alleged in the bill would be in violation of such pleaded constitutional restrictions.

The federal questions were raised again upon the second appeal to the Supreme Court of Florida because at that time the same identical bill of complaint containing such federal questions was again before the court. The fact that the opinion of the Supreme Court of Florida upon the second appeal failed to refer specifically to the federal questions cannot destroy the effect of the manner in which the federal questions were raised and presented to the Court. Under such circumstances, it has been settled by this court that federal questions were properly raised. *New York*

ex rel. Bryant v. *Zimmerman, et al.*, 278 U. S. 63. *Dewey* v. *City of Des Moines*, 173 U. S. 193. *Cissna* v. *Tennessee*, 246 U. S. 289. *Dickenson* v. *Stiles*, 246 U. S. 631.

The contention of the Appellees that the federal questions were not raised or decided by either the trial court or the Supreme Court of the State of Florida is equally unsound. This is so because the determination of the federal questions raised in the bill of complaint was necessarily involved in the disposition of the case by the trial and appellate court and the necessary effect of the decision on the second appeal has been to deny the federal claims asserted. *Kaukauna Water Power Co.* v. *Green Bay and Miss. Canal Co.*, 142 U. S. 254. *New York, ex rel Bryant* v. *Zimmerman, et al.*, 278 U. S. 63.

The opinion of the Supreme Court of Florida upon the second appeal shows that the decision rested not upon want of proof of particular facts, but upon the erroneous application of the law by that court to certain established facts. The reasons given by the court are: (1) "The customer resides in Florida," (2) "The original payment was made by him in Florida at the branch office," (3) "Interest and brokerage commissions are paid in Florida," (4) "Florida law protects the branch office and business transactions therein," (5) "Florida courts provide forums for adjudication of grounds arising out of the transactions." Each of those assigned reasons appeared from the bill itself, and no question of proof or want of proof is involved in any of them. Indeed, even if the Supreme Court of Florida had said in its second opinion, "Every allegation of the bill has been proved," it could still have made the same five observations.

Therefore, said decision that the debit balances or accounts receivable "Originated" in Florida and by that fact were localized for taxation, notwithstanding all other facts alleged and proved in regard thereto, necessarily

had the effect of holding that taxation of the intangibles, in the situation presented, was not a denial of the federal claims asserted by the plaintiffs. Those assigned reasons of the Florida Supreme Court wholly ignored the allegations of the bill and the proof to the effect that the intangibles never became an integral part of any independent business conducted by the Appellants in Florida, and the many other factors relied on by plaintiffs as placing the property outside of Florida.

The Florida Supreme Court's decision could only have been reached on one of the following three bases: (1) Domicile of the plaintiff stock brokerage firm in the State of Florida; or (2) A business situs for the intangibles in question in the State of Florida; or (3) The erroneous view (held by the trial court) that the doing of some business in Florida by the New York firm would justify taxation of foreign held intangibles, as in the case of an excise tax.

The decision was not on the first basis mentioned. The Florida Court did not hold that the plaintiffs failed to show that the firm of Thomson & McKinnon, a New York partnership, was a non-resident of Florida. There is no holding that the plaintiff partnership is domiciled in Florida. The theory expressed by the court was that it viewed the debit balances as being within the State of Florida, and therefore owned *in* Florida and not owned *in* New York.

If the decision was predicated on the second basis mentioned, that of a Florida business situs for the intangibles, the reasons which the court assigned obviously could not support such a holding because they ignore the established standards and requirements for determination of business situs, and because they disregard the showing, by allegation and proof, that the intangibles were not localized by becoming an integral part of any independent business in the State of Florida, did not form a part of the firm's capital in Florida, were not the product or subject of any

loans made within that State, and that the agents of the firm in Florida acted only in a clerical and ministerial capacity in soliciting customers for foreign brokerage transactions and were without authority to lend money or to enforce collection of the accounts in question or to use or handle the proceeds thereof other than to transmit them to New York where such assets were a part of the firm's general capital. A judicial determination that intangibles of a non-resident have a business situs in a State apart from the State of the owner's domicile inescapably involves the question of constitutionality under the Fourteenth Amendment.

If the decision was predicated on the third basis, mentioned above, on the theory that the doing of some business in Florida by the plaintiff New York brokerage firm is enough to sanction the taxation of intangibles accruing to the firm as a result thereof, in spite of the fact that such intangibles do not have a business situs in Florida, then the federal questions asserted are necessarily raised, because (a) the attempt is to tax property admittedly beyond the State's jurisdiction, in violation of the due process clause, and (b) because the standard thus applied to non-residents is different from that which said court in *Hunt* v. *Turner*, 54 Fla. 654, 45 So. 509, has announced is applicable to Florida residents, resulting in a denial of equal protection of the laws.

The entire first section of the Appellees' statement is based upon the false premise that the tax sought to be enjoined is in the nature of an income, privilege, or excise tax which becomes proper upon a mere showing that Thomson & McKinnon do some business within the State of Florida. The tax sought to be imposed and to which the Appellants object is a general ad valorem tax on intangible personal property. (See Appellants' Statement under Rule 12). It is leviable only upon property *in* the

State of Florida or owned by persons *residing* in the State of Florida. (See paragraph 2 Appellants' Jurisdictional Statement.)

The Supreme Court of the State of Florida regardless of its announced reasons has in effect held that by accepting orders through a branch office in Florida and there rendering certain perfunctory services of a clerical and ministerial nature, purely non-discretionary in character, the Appellants have placed the debit balances, owing from such of the firm's customers as avail themselves of these facilities, under the taxable jurisdiction of the State of Florida; and this although by every previously existing legal test the intangibles mentioned have acquired no business situs in Florida.

It is not necessary to look beyond the two opinions of the Supreme Court of Florida (Exhibits 1 and 2 to Appellants' Jurisdictional Statement) to perceive this to be so. As has been stated in an *Annotation in 143 ALR 361, at page 383,* the Florida Supreme Court in its first opinion held that the utter lack of discretion in the Florida branch agencies denied the debit balances a business situs in Florida.

> "• • • In Smith *v.* Lummus (1942)—Fla.——6 So (2d) 625, a partnership domiciled outside the state conducted its business as commission broker for the purchase and sale of securities from its main office but kept a branch agency within the state for taking orders for the purchase and sale of stocks and for giving information to prospective customers. The agents could only receive orders for stock transactions and accept payments from customers but they had no power to pass on the credit standing of anyone who applied to buy stock on margin nor to do anything with the money they received other than deposit it in a bank to the partnership's account. An entirely separate account was kept for the purpose of paying salaries and op-

erating expenses of the branch agency. The court, coming to the 'inescapable conclusion' that the agents exercised no discretion whatever and performed purely ministerial duties, concluded that the agency was not self-operating and did not constitute an independent business, and that therefore it did not have a situs within the state so as to be subject to personal property tax. The decision clearly shows that the extent of the authority of the local agent was the decisive factor in the mind of the court in determining whether the credits extended to customers dealing with the partnership through the agency had a business situs in the State for the purpose of taxation. 'It is conceivable', the court declared, 'that one in a business like that conducted by the plaintiffs (the partnership) could establish an office in a state other than the domicil, provide a fund there to be used by representatives in the purchase of stock and in financing customers with authority on the part of the representative to draw upon their business judgment and discretion in the operation of the business, and thereupon become liable to taxation upon the property of the enterprise. That, however, is not the situation with which we are dealing. * * * In the general business affairs of the plaintiff there are many features calling for the exercise of judgment and discretion. All of those features are absent from deals made in Florida (the state where the agency was situated). We iterate when we call attention of the reader to the averments that the representatives of the firm in this state exercise none of such judgment or discretion but simply perform the clerical services incident to the business. * * * And we think the restricted operation here refutes the argument that there is a business situs so distinct that taxation on intangibles is justified."

In this opinion the Florida court said:

"If we are to follow the rule which we stated at the outset, with reference to taxation at the situs, the

State officials would go beyond the sphere of their authority if they assessed and collected taxes on the debit balances when *all save certain mechanical activities with reference to them* are, according to the allegations of the bill of complaint, controlled entirely from another state." (See Exhibit 1 to Appellants' Jurisdictional Statement).

Later, in its opinion on the second appeal, as noted, a majority of the Court enumerated a few of those same "mechanical activities" as necessitating a conclusion that the debit balances are taxable by the State of Florida. Such a conclusion forces the Appellants to pay an illegal assessment upon property beyond that State's jurisdiction, and this is contrary to the prohibitions of the Federal Constitution.

Union Refrigerator Transit Company v. *Kent,* 199 U. S. 194;

Safe Deposit & Trust Company v. *Virginia,* 280 U. S. 83;

Curry v. *McCanless,* 307 U. S. 357.

The Supreme Court of Florida, despite its assertion to the contrary, has said, in effect, that even if the property is without the jurisdiction of the State of Florida she may lawfully tax it. Such a ruling presents a Federal question for the proper consideration of this Honorable Court. This Court has held many times that it must itself determine whether or not a Federal question is involved and for such purpose will examine the record.

U. S. v. *Pink, Supt. of Insurance State of New York,* 315 U. S. 203, 62 S. Ct. 552 @ 559.

"This Court will review or independently determine all questions on which a federal right is necessarily dependent. U. S. *v.* Ansonia Brass & Copper Co., 218 U. S. 452, 462, 463, 471, 31 S. Ct. 49, 50, 51, 54;

54, L. Ed. 1107; Ancient Egyptian Order *v.* Michaux 279 U. S. 737, 744, 745, 49 S. Ct. 485, 488, 73 L. Ed. 931; Broad River Power Co. *v.* South Carolina 281 U. S. 537, 540, 50 S. Ct. 401, 402, 74 L. Ed. 1023; Pierre *v.* Louisiana, 306 U. S. 354, 358, 59 S. Ct. 536, 83 L. Ed. 757.

Honeyman v. *Hanan,* 300 U. S. 14, 57 S. Ct. 350 @ 352.

> "As this Court must decide whether it has jurisdiction in a particular case this Court must determine whether the federal question was necessarily passed upon by the state court. That determination must rest upon an examination of the record."

The conclusion of the Florida Supreme Court that the Plaintiffs, Appellants, failed to prove the bill is unfounded.

All of the material elements concerning the conduct of Appellants' business, as alleged in the bill, coincide with those disclosed by the testimony and exhibits constituting the proof in this case, and every such element is proven. The weight and sufficiency of one witness' testimony has been held adequate to support the burden of proof in a law suit. The law adopted by the Supreme Court of Florida in the case of *Jacksonville Traction Co.* v. *Greene,* 151 So. 523, 113 Fla. 316, is:

> "Plaintiffs' uncorroborated testimony, if reasonable, can carry the burden of proof unless contradictory evidence was so strong and positive that a verdict approving a single witness is clearly against the manifest weight of the evidence."

The proof in this case is plentiful to convince an open mind, and the law does not require that it meet the burden of convincing a prejudiced one *(20 Am Jr. 1026),* nor that each element be established as a certainty to the exclusion of every other possibility.

"In order to arrive at a conclusion upon a question of fact, the rule of evidence does not require that there should be that amount of certainty which will exclude the possibility that the fact can be otherwise, but only that it shall be of such a degree, induced by appropriate evidence, as will produce moral conviction."

Smith v. *Croom*, 7 Fla. 81.

The testimony of Mr. Kiernan is not unduly extensive. The complete transcript of his examination, both direct and cross, is set out in the record (R. 49-104). This testimony, together with the exhibits contained in Appendix A (R. Appendix A, 1-45), constitutes the evidence in this cause. Since this Honorable Court, itself, will want to examine the evidence, we would like to point out that all of the particular allegations referred to in the first opinion of the Florida Supreme Court were proved by positive and undisputed testimony.

1. Domicile and centralization of the brokerage business in New York was shown (R. 49-54, and Exhibits 1 and 6 at pages 1 and 43 of Appendix A).

2. Plaintiffs are commission brokers, not dealers (R. 53).

3. The branch offices, or agencies, merely solicit business (R. 56 and 80), and cannot trade directly on any exchange (R. 65 and 79).

4. The agencies furnish quotations and statistical data and other assistance to customers desiring to place orders (R. 57), and accept and send orders to the main office for execution (R. 63 and 65).

5. The attempted application of the general intangible tax law to the challenged tax was admitted by answer.

6. The debit balances have no reference to property "brought into the State or held or owned in the State" (R. 73).

7. "No merchandise or stock in trade" is sold here (R. 73).

8. Debit balances arise in margin accounts only (R. 54) on margin purchases, and not on margin (short) sales (R. 62).

9. A debit balance is an obligation of a customer which arises when payment is made, in New York, by the firm, to a third party, for the account of the customer, of the price of the stock (R. 66, 67, 68, 74).

10. The debit balance is not to be confused with the margin or customer's equity. The margin, or part of the purchase price furnished by the customer, is his "equity". The balance of the price, advanced for him by the firm in New York at the time delivery of stock is accepted by the firm, is the debit balance resulting from the purchase for his account (R. 62 and 68).

11. Before the customer can trade he must fill out a confidential report, and be accepted by a partner of the firm resident and active in the New York office (R. 57-58, and Exhibit 2 at page 35, Appendix A). A branch office cannot pass on a new customer (R. 58-59).

12. He must then sign what is known as an hypothecation agreement (R. 60-61, and Exhibit 4 at page 39, Appendix A). New York law requires this for the customer's securities to be pledged or commingled by the broker (R. 61).

13. The hypothecation agreement does not contain any promise to pay any debit balance. No money is owed by the customer upon signing it (R. 62). It does not compel the customer to trade (R. 62), nor does it compel the broker to execute an order for a trade if the broker has any reason for refusing it (R. 64).

14. The hypothecation agreement (Exhibit 4 at page 39, Appendix A) simply states the terms under which margin transactions, and principally the collateral thereof, will be handled, if and when any margin purchases or sales are made for the customer's account.

15. "These loans are made only in another state and never in the State of Florida." That has reference to the customer's obligations from advances for his account. This was proved by showing:

(a) No advances are made to a customer (R. 68 and 73);

(b) The Florida agents make no loans (R. 71 and 76);

(c) The Florida credits are restricted to "debit balances" resulting from purchases for the account of margin customers (R. 74);

(d) The exchanges where the payments are made by the firm which give rise to the customer's obligation to repay the advances are all located outside the State of Florida (R. 74). Ninety-nine per cent of the trading is on the New York Stock Exchange (R. 63);

(e) The placing of an order for a purchase on margin does not obligate the customer or create a debit balance, and nothing is owed when the trade is made on the exchange by brokers (R. 66);

(f) Nothing is owed by the customer until such time as the firm actually advances the purchase money (margin amount plus excess over margin) some time within two days after the exchange floor transaction (R. 67-68);

(g) These advances (ninety-nine per cent of them) are made in New York, to the seller of the stock, for the benefit of the customer (R. 74), or at the places where other, out-of-state exchanges are located (R. 74).

16. "No money or capital forming the source of such loans to customers is kept in this State" (R. 68 and 73).

17. "When such loans are made they are not evidenced by promissory notes or other writing (proved at R. 61 and 74) and are secured by retention of the securities in New York with the right in the broker of transferring them for its protection" (R. 68, 69, 71, 75, 102).

18. "The stocks, on which the firm has advanced part of the purchase price and, which it holds to secure the payment of the remainder due by the customer, are held in the foreign state." (R. 68).

19. "The debt 'is created by and under the laws of the State of New York, and independent of the laws of Florida.'" (R. 65-66 and 74).

20. "The copartnership does not resort to the laws of Florida to effect collection of debit balances, and the so-called agencies are not authorized to collect amounts." This was supported by evidence as follows:

(a) The branch offices are not authorized to collect a debit balance (R. 75).

(b) The firm has never sued a customer here (R. 75 and 88).

(c) Collection, where necessary to be enforced, is made by sale of collateral (R. 75 and 97).

21. "There is no competition with any business in Florida and the debit balances are not the result of any loans made by any representative here." This was shown as follows:

(a) The business is that of acting as commission broker on a stock or commodity exchange (R. 53). The branch office solicits such business (R. 56).

(b) There are no such exchanges in this state (R. 54).

(c) The purchases made for customers could not be handled by local businesses such as banks except through this or some other New York Resident Stock Exchange Member firm (R. 65 and 76).

(d) The distinction between this case and a branch store or branch office for local loans (which would compete with local merchants and local loan businesses) was brought out by showing that the firm is not a "dealer" and does not sell stocks to its cus-

tomers (R. 53), does not sell merchandise in this State (R. 73), and no money is advanced directly to customers or loans made in this State (R. 68, 71, 73, 74, 76).

22. "Whenever a customer wishes to pay to the firm any money in 'reduction or discharge of a debit balance, or for margin or additional margin,' he may deliver the money to the Florida agent who gives him in exchange a temporary receipt but the agent has no authority or control over the money received except to send it intact to New York or to place it in a bank account from which it may be withdrawn only by the principal office" (R. 76-77).

23. "Upon notice from the agent the customer's account in New York is then credited immediately with the amount of the payment." (R. 77-78).

24. "None of the moneys received by the agents may be applied by them to the expenses of the agency, funds for that purpose being supplied out of the firm's general capital and held in a local bank account separate from moneys paid to the firm by customers" (R. 77).

25. "All records of customers' accounts are kept at the home office and it is from there that all formal notices, reports of transactions and statements are furnished." (R. 73 and 76).

26. "Approval and acceptance of customers is made entirely in New York and with reference to these matters agents in Florida have no authority" (R. 57-59).

27. "In the conduct of its business the copartnership complies with the rules of the New York Stock Exchange and other exchanges, requirements of the laws of the State of New York and the acts of Congress" (R. 57-61 and 65).

In the final analysis an examination of the testimony and exhibits is, of course, the only possible means of verifying that every material allegation of ultimate fact in the bill of complaint is supported in the record by competent, uncontroverted evidence, (R. 1-16; 49-104 Appendix A).

Different conclusions were drawn from these facts by the Supreme Court of Florida in its first and second opinions. In the first opinion the Court unanimously found the intangibles involved possessed no business situs within the State of Florida. A change in the membership of the Court occurred before the second appeal was heard. Mr. Justice James B. Whitfield, after more than thirty years on the bench, resigned. His successor, not having heard the first appeal, held contrary, and his vote in favor of taxation gave the 4 to 3 majority on the second appeal. It is this last determination which we assert violates the constitutional guaranties asserted by the plaintiffs.

We, therefore, submit that the question of whether or not the State of Florida can deprive Appellants of property by levying and collecting a tax beyond that state's jurisdiction is not only raised but is moreover so inextricably intertwined with the heart and marrow of this litigation as to defy separation. No decision can be rendered herein, we feel, which does not unalterably affect the constitutional rights duly invoked by Appellants.

II.

The Questions Involved Are Substantial.

One way of determining whether or not the questions involved in this Appeal are substantial is to review what questions are presented. Fundamentally there is but one question, viz., Can the State of Florida lawfully tax certain intangibles owned by Plaintiffs, Appellants, a New York stock brokerage firm? The determination of this depends in turn upon whether or not the State of Florida has acquired taxable jurisdiction over the intangibles in question or, do these particular intangibles have a business situs within the State of Florida. In short the ultimate determination of the question thus rests upon the examination

of the individual facts of this particular case. This Court has consistently recognized such a problem as constituting a substantial and proper question for its determination.

It is true that this Honorable Court has held many times in various cases that the intangibles involved in those cases possessed a business situs within a given state seeking to tax them. It is likewise true that the court has many times held that various taxes were properly imposed by one state upon the citizens and residents of another because of the nature of the tax or some other factor besides business situs. This is the case with every single one of the citations offered by the Appellees in their "Statement as to the Jurisdiction and Motion to Dismiss" as a refutation of the substantiality of the questions raised upon this Appeal. The cases of *Metropolitan Life Ins. Co.* v. *New Orleans*, 205 U. S. 395, 27 S. Ct. 499, 51 L. Ed. 853, and *Liverpool & L. & G. Ins.* v. *Board of Assessors*, 221 U. S. 346, 55 L. Ed. 762, 31 S. Ct. 550, involved a taxing statute specifically directing the assessment of non-residents capital whether located within the State of Louisiana or not. *Wisconsin* v. *J. C. Penney Co.*, 311 U. S. 435, 61 S. Ct. 246, 85 L. Ed. 267, 130 A. L. R. 1229 involved an income tax. *Curry* v. *McCanless*, 307 U. S. 357, 83 L. Ed. 1339, 59 S. Ct. 900, 123 A. L. R. 162 involved a transfer tax at death.

In the Mississippi cases of *Stone* v. *General Contract Purchase Corporation*, 7 So. 2d 806; *C. I. T. Corporation* v. *Stone*, 7 So. 2d 811; *Stone* v. *General Electric Contracts Corporation*, 7 So. 2d 811; *Stone* v. *Universal Credit Co.*, 7 So. 2d 820; *Stone* v. *Yellow Manufacturing Acceptance Corporation*, 7 So. 2d 820, which this Honorable Court affirmed in 87 L. Ed. 23, et seq., the statutory levy was of a "privilege tax"; and finally in the case of *Utah* v. *Aldrich*, 316 U. S. 172, 86 L. Ed. 1358, 62 S. Ct. 1009, the tax involved was by the State of Utah upon a transfer of the shares of stock in a Utah Corporation, another excise tax.

This Court has never held, however, nor had any State Court prior to the decision here under consideration, that the debit balances arising from the business operations of a foreign domiciled stock brokerage firm are subject to a general ad valorem tax by the state of domicile of the firm's customers where such debit balances are neither held, owned, nor by existing legal tests possess a business situs within the said state.

For these reasons, because the unanimous first opinion of the Supreme Court of Florida so indicates, and because of the 4 to 3 vote on the decision appealed from, we believe that the question raised by this Appeal is substantial.

Moreover, if the opinion of the Supreme Court of Florida from which we are appealing herein is adopted as the law by her sister states a new and onerous burden will be placed upon the nation's financial structure. The extent to which the stock brokerage business affects the economic life of the nation is a matter of common knowledge. An open invitation to forty-seven such additional taxing authorities to collect tribute from such operations must inevitably have a deleterious effect. This Court should examine the facts of this case to determine whether the 14th Amendment will permit such a levy.

Respectfully submitted,

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